

There was a provocative article in this weekend's *Wall Street Journal* titled, "How to Play a Market Rally." The authors' use of the word "play" appears to indicate that they think that successful investing is like going to Las Vegas. In the article, the time-tested practice of buy and hold is declared dead as from the period December 24, 1998 through November 11, 2010, had you remained invested in the S&P 500 you would have had zero appreciation. Actually, you would have had a depreciation of 1%, but once including dividends, your total return would have been roughly 19%, or about 1.48% annually, certainly nothing to write home about.

The writers go on to enlighten us of two alternative strategies. Had an investor sold one-tenth of his or her portfolio every time the market gained 20%, and then allocated one fifth of his cash to the market when stocks declined more than 10%, they would have gained 14% over the same period, presumably without considering dividend income. Even with dividends (which you are obviously not entitled when you sell out of the market) the total return would have been roughly 33%, or 2.37% annually.

Another foolproof strategy (at least in this back tested time period) was to sell 10% of your portfolio at the end of each month in which the stock-market capitalization to Gross Domestic Product ratio was above 115%. The investor should then purchase stocks with 20% of previously raised cash when the ratio fell below 75%. This discombobulated strategy produced a gain of 36.5%, and adding dividends the total return amounts to roughly 54%, or 3.71% annually.

With all due respect to the back testing wizards of the financial media, we at Resource Consulting Group believe that buy and hold is indeed not dead. (Highly acclaimed economist and professor at Princeton University, Burton Malkiel, agrees in his opinion published in the November 18<sup>th</sup> issue of the *Wall Street Journal*.) The goal should be to properly formulate an investment policy with an appropriate investment allocation and stick to it. In this example, had you been fully invested in a broadly diversified pool of equity securities from 12/31/98 through 10/31/10 (note that the time periods vary by several days due to the use of month-end valuations, however any performance difference is nominal over the twelve year period) you would have enjoyed a total return of 118%, or 6.83% annually.

To quantify the difference to investors, had you invested \$1,000,000 in each of the referenced strategies your results would have been:

- 1) Buying & holding the S&P 500 would have generated a profit of \$190,000.
- 2) Buying on dips and selling on gains would have generated a profit of \$333,000.
- 3) Using stock market capitalization relative to GDP would have earned you \$540,000.
- 4) Buying and holding a globally diversified portfolio would have resulted in a gain of \$1,180,000.

Although these results do not include management costs and taxation, it doesn't take a math wizard to see which of these strategies should be declared dead.

If this isn't enough proof enough for you, a statistical analysis titled, "Quantitative Analysis of Investor Behavior 2009" was performed by the independent consulting firm Dalbar, Inc. The analysis finds that the average investor, through a combination of market timing and chasing hot stocks and funds, returned on average 3.17% annually from January 1990 through December 2009. Had you simply bought the S&P 500 and held it over the same time period you would have returned 8.21% annually. A fully diversified portfolio would have done even better.

Long live "buy and hold" and continued success to the patient investor!

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*We are the largest fee-only financial planning  
and investment management firm in Florida.*



Resource Consulting Group  
PO Box 4930  
301 E Pine Street, Suite 300  
Orlando FL 32802  
Phone: 407/422-0252  
Fax: 407/649-8795  
Website: [www.resourceconsulting.com](http://www.resourceconsulting.com)